

DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 04-0197
Use Tax
For the Periods 2000 - 2002

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ISSUE

I. Sales and Use Tax—Production exemption

Authority: IC 6-8.1-5-1(b); IC 6-2.5-3-2; IC 6-2.5-3-4; IC 6-2.5-3-5; IC 6-2.5-5; IC 6-2.5-5-3(b); Indiana Dept. of Revenue v. Interstate Warehousing, Inc., 783 N.E.2d 248, 250 (Ind. 2003).

Taxpayer protests the assessment of use tax due on items Taxpayer asserts are used in production.

STATEMENT OF FACTS

Taxpayer manufactures and sells pharmaceutical products. The Department conducted an audit of Taxpayer and assessed use tax due on items that were purchased exempt from sales tax, but upon which the auditor found use tax should have been paid. Taxpayer filed a protest and a hearing was held.

I. Sales and Use Tax—Production exemption

DISCUSSION

All tax assessments are presumed to be accurate; the taxpayer bears the burden of proving that an assessment is incorrect. IC 6-8.1-5-1(b).

Taxpayer purchased a pump to pump water from the ground. Taxpayer is on a well and uses the water to make products as well as for general purposes. Taxpayer asserts that pumping the water from the ground is an integral part of manufacturing. The auditor determined that the pump was used in pre-production.

IC 6-2.5-3-2 imposes an excise tax, commonly called the use tax, on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that

transaction. Credit against the use tax due is given for sales tax that already has been paid. *See* IC 6-2.5-3-4 and IC 6-2.5-3-5.

Exemptions to sales and use tax exist. *See, generally*, IC 6-2.5-5. The Indiana Supreme Court has stated that it is well established that exemption statutes are strictly construed against a taxpayer so long as the intent and purpose of the Indiana Legislature is not thwarted; as such, a taxpayer has the burden of establishing its entitlement to an exemption. Indiana Dept. of Revenue v. Interstate Warehousing, Inc., 783 N.E.2d 248, 250 (Ind. 2003). IC 6-2.5-5-3(b) states that transactions involving manufacturing machinery, tools, and equipment are exempt from the sales and use tax if the person acquiring the property acquires it for direct use in the direct production, manufacture, fabrication, assembly, extraction, mining, processing, refining, or finishing of other tangible personal property. The pump brings water from the ground to a pressure tank and the water then is distributed throughout the building for general purpose uses as well as in manufactured products. The pump is not used to distribute water within the manufacturing process, but before the manufacturing process. For this reason, the purchase of the pump was not exempt from sales and use tax.

Taxpayer also subscribed to United States Pharmacopoeia (USP)—a book that provides standardized test methods for the most common and widely used raw materials. Taxpayer stated that the testing of raw materials is essential and mandated; for this reason the subscription should not be taxed. However, because USP contains the specifications for testing raw materials when received and before combination with other ingredients or processes, the USP book was used before the manufacturing process. For this reason, the purchase of the subscription was not exempt from sales and use tax.

Taxpayer also had purchased lab supplies and materials and did not pay sales or use tax on those transactions. During the audit, Taxpayer and the auditor agreed that 70% of the lab supplies were used in an exempt manner and 30% of the lab supplies were used in a taxable manner. Taxpayer later asserted that the lab supplies and materials were used in production. At the hearing, Taxpayer returned to the original determination agreement.

FINDING

For the reasons stated above, Taxpayer's protest of the taxability of the well pump and the USP subscription is denied; use tax is due. In accord with the audit agreement, 70% of the lab supplies and materials are not taxable and 30% are taxable.